
Paying for College Today

For many Americans, providing a college education for their children has long been an important family goal. Paying for that education, however, has never been easy. Over the past few years it has become even more of a challenge as college costs continue to rise.¹

Few families seem able to save enough to fully fund four or more years of higher education. For many students, some type of financial aid, in the form of grants, scholarships, loans, or work-study, is needed to make the dream a reality.

And such financial aid is available. The federal government, through the Department of Education, provides more than \$120 billion a year² in student aid, through a variety of programs. Private organizations and foundations, state governments, as well as the schools and universities themselves, are additional sources of financial aid.

Applying for Financial Aid

The vast majority of financial aid is awarded through a standardized process which, in general, proceeds as follows:

- **Free Application for Federal Student Aid (FAFSA):** The student and his or her family complete the Free Application for Federal Student Aid, the single form used to apply for all types of federal aid; it is also used to apply for state financial aid at many public and private colleges. The FAFSA collects information such as family size and number of family members in college, in addition to financial data such as income and benefits, and net assets.
- **Student Aid Report (SAR):** Using the information supplied on the FAFSA, the government calculates the amount a family is expected to contribute toward a student's education, known as the Expected Family Contribution (EFC). This information is reported on the SAR and is sent to the student. The same information is sent to the financial aid offices of the colleges the student listed on the FAFSA.
- **CSS/Financial Aid PROFILE:** A few schools will require a prospective student to complete an additional standardized financial questionnaire known as PROFILE. The data collected on this form is used to award a college's institutional aid.

¹ See "Trends in College Pricing – 2021," published by The College Board, page 12, Figure CP-2 - Published Tuition and Fees Over Time.

² Source: Department of Education website: <https://www2.ed.gov/about/offices/list/rsa/index.html>, accessed November 8, 2021.

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- **Cost of attendance:** To calculate financial aid eligibility, colleges need to first determine the cost of attendance at the institution. The cost of attendance includes, in addition to tuition and fees and books, general living expenses such as rent or dormitory costs, transportation, and personal expenses a student could be expected to incur during the nine-month academic year.
- **Financial aid eligibility or financial need:** Eligibility for need-based financial aid is determined by taking the college's calculated cost of attendance and subtracting the EFC. The difference, if any, is the amount the student may receive in need-based forms of financial aid, including grants, scholarships, and loans.
- **Financial aid package:** Once the need-based eligibility is determined, a college's financial aid office will attempt to provide for that need with a combination or package of financial aid funds that may include grants, loans, scholarships, and work-study funds. The amount and type of financial aid will vary between colleges. In some cases a financial aid package may not cover all costs, leaving a gap that the student and his or her family must cover from other sources.

Federal Financial Aid

A major source of financial aid provided to college students in the U.S. is from programs funded and/or administered by the federal government, with much of the support coming in the form of student loans. The major elements in federal student aid are:

- **Federal Pell Grants:** Pell Grants are designed to assist very low-income undergraduate students and are awarded based on expected family contribution (EFC). Only students with very low EFCs are awarded Pell Grants. Pell Grants do not have to be repaid.
- **Federal Supplemental Educational Opportunity Grant (FSEOG):** Like Pell grants, FSEOGs do not have to be repaid. They are awarded to undergraduate students with exceptional financial need.
- **Teacher Education Assistance for College and Higher Education (TEACH) Grant:** A federal grant to students who agree to teach for four years at an elementary school, secondary school, or educational service agency that serves students. If a grantee does not complete his or her service obligation, the TEACH grant is converted to a Direct Unsubsidized Loan with interest due from the date the TEACH grant was disbursed.

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- **Iraq and Afghanistan Service Grant:** A grant awarded to limited group of individuals whose parent or guardian was a member of the U.S. armed forces and who died as a result of military service performed in Iraq or Afghanistan after the events of 9/11. Other requirements apply.
- **The William D. Ford Direct Loan Program:** This program is the Department of Education’s main loan program. Direct subsidized loans are made of the basis of financial need. They do not accrue interest nor require repayment until six months after the student ceases to attend college at least half time. Direct unsubsidized loans are not based on need and interest accrues from the date the loan is disbursed. Direct PLUS loans are loans made to graduate or professional students and to parents of dependent undergraduate students to help pay for education expenses not covered by other financial aid. Interest accrues from the date the funds are disbursed, but repayment is not required until six months after the student ceases to attend college at least half time. Direct Consolidation loans allow a student to combine all of his or her eligible federal student loans into a single loan; repayment begins within 60 days of the loan being disbursed.
- **Federal Perkins Loans:** Perkins loans are federal low-interest loans. They are awarded based on need and the availability of funds. No interest accrues while the student is attending school at least half time. Repayment begins nine months after the student ceases to attend school at least half time.
- **Coronavirus Aid, Relief, and Economic Security (CARES) Act:** The CARES Act provided relief for student loan borrowers whose debt was owned by the U.S. Department of Education. For the period from March 13, 2020 to September 30, 2020 these loans were placed in “administrative forbearance,” with a 0% rate of interest, allowing borrowers to stop making loan payments. Generally, this provision applied to (1) defaulted and non-defaulted Direct Loans; (2) Defaulted and non-defaulted FFEL Program loan; and (3) Federal Perkins Loans.¹
- **Federal Work-Study Program (FWS):** The FWS program provides federally funded employment for qualified students in both on-campus and off-campus positions. The amount a student can earn is limited to the amount of the award.

¹ Some FFEL Program Loans are owned by commercial lenders. Some Perkins Loans are owned by educational institutions. These loans are not covered by the “administrative forbearance” proved in the CARES Act.

Other Financial Aid Programs

In addition to the financial aid programs provided through the federal government, there is a wide range of aid available through other organizations.

- **State programs:** Many state governments have their own financial aid programs. Such programs include need-based grants (the family has to show financial aid eligibility), as well as work-study programs, loan-forgiveness programs for targeted careers, and merit-based scholarship programs.
- **Institutional aid programs:** Many schools have additional means of making college affordable. Scholarships, based on either academic or athletic ability, are one example. Some schools have their own student loan programs to replace or supplement federal loan programs. Some institutions offer installment or deferred payment plans for tuition, or a discount may be offered if more than one child from the same family is enrolled, or if the parents are alumni.
- **Military aid programs:** The Armed Forces have available a number of programs to enable prospective, active duty, and former service personnel to attend college. Reserve Officer Training Corps (ROTC) scholarships are available at a number of schools. A ROTC/NROTC Scholarship or an appointment to one of the service academies, West Point, Annapolis, or the Air Force Academy effectively ends any concerns about paying for college. Current active duty personnel can apply for tuition assistance through their education officer. For veterans, the various GI Bills and the Army or Navy college savings funds are additional sources of financing.
- **Private scholarships:** Many private organizations make available scholarships, based on both need and merit. Many scholarships are for relatively small amounts of money or for only a single year and a student may need to apply to many different scholarship programs. Scholarship information is widely available at bookstores and libraries, in high school and college financial aid offices and on the Internet.

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Tax Advantaged Strategies

Congress has passed legislation¹ designed to lighten the burden of paying for higher education. Because the rules surrounding these strategies can be complicated, the counsel of a qualified tax or financial professional is recommended.

- **Education tax credits:** Two separate tax credits are available: (1) the American Opportunity Tax Credit, of up to \$2,500 per student, per year, for tuition and fees paid during the first four calendar years of college, and (2) the Lifetime Learning Credit, providing a credit of up to \$2,000 per return for qualified education expenses. A taxpayer may not take both credits in the same year. Other limitations and restrictions apply.
- **Interest deduction on education loans:** A deduction of up to \$2,500, taken as an adjustment to gross income, is available for interest paid on student loans. Certain restrictions and requirements apply.
- **Exclusion of U.S. Savings Bond interest:** Interest earned on U.S. Savings Bonds is normally taxable. However, if a taxpayer pays qualified education expenses, the interest earned on qualified U.S. savings bonds may be excluded from income. Certain income level and filing status requirements apply.
- **Withdrawals from IRAs:** Withdrawals from *traditional IRAs* used to pay qualified education expenses are exempt from the 10% penalty on withdrawals before age 59½. However, such withdrawals are generally subject to ordinary income tax. If certain requirements are met, withdrawals from *Roth IRAs* for any purpose may be made tax and penalty free.

Other Approaches

A number of other approaches can be used to help pay for college expenses. Consider

¹ The rules discussed here concern federal income tax law; state or local law may vary.

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carefully the pros and cons of each suggestion, including the income tax ramifications, the impact on any possible financial aid, the likelihood that a student might not complete college, and any effect on your long-term financial goals.

- **Home equity loan:** Parents with equity in the family home may want to consider taking out a home equity loan.
- **Life insurance cash values:** Cash-value life insurance policies can provide another source of low-cost loans.¹
- **Borrow from qualified plans:** Some types of employer-sponsored qualified plans allow a participant to borrow from the plan. There are generally strict rules regarding the repayment of such loans.
- **Skip a year:** Some colleges will admit a student and defer admission allowing the student to live at home, work full-time and save the earnings for college.
- **Live at home and commute:** A family can save thousands of dollars a year by having a student live at home and commute to school.
- **Choose a lower cost school:** State-supported public colleges and universities generally charge a lower tuition for in-state residents. To further save money, some students begin their studies at less expensive community or junior colleges and then transfer to a four-year school to complete their degree.

Other Resources

There are a number of published references and guides to paying for college available in bookstores and public libraries. In addition to providing a wide range of reference materials, many high schools and colleges offer free financial aid seminars presented by professional financial aid administrators. The state and federal agencies involved in higher education are also excellent sources of information.

On the internet, there are a number of websites which can provide information.

- **The College Board:** <https://www.collegeboard.org>
- **FinAid:** <https://www.finaid.org>

¹ Loans from a cash-value life insurance policy will reduce the available death benefit. If a policy lapses or is surrendered with a loan outstanding, the loan will be treated as taxable income in the current year, to the extent of gain in the policy. Also, policies considered to be modified endowment contracts (MECs) are subject to special rules.

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- **U.S. Department of Education – student aid website:** <https://studentaid.gov/>
- **Free Application for Federal Student Aid (FAFSA):** <https://studentaid.ed.gov/sa/fafsa>
- **CSS/Financial Aid Profile®:** <https://studentaid.gov/h/apply-for-aid/fafsa>

Begin Early and Seek Professional Guidance

The key step in paying for a child's education is to begin the process as early as possible. A great deal of information, as well as counseling, is available from high schools, colleges and the various government agencies involved in higher education, at little or no cost. Questions involving income, gift, or estate taxes should be carefully reviewed with a Certified Public Accountant (CPA), IRS Enrolled Agent (EA), legal counsel or other qualified professionals.